Supreme Court, U.S.
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No. 96-1785

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1996

DISCON INCORPORATED,

*Cross-Petitioner*,

v.

NYNEX CORPORATION, NYNEX MATERIEL ENTERPRISES COMPANY, NEW YORK TELEPHONE COMPANY, ROBERT J. ECKENRODE, and BERNARD O'REILLY,

*Cross-Respondents*.

ON CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

## BRIEF IN OPPOSITION TO CONDITIONAL CROSS-PETITION

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June 13, 1997

## Counter-Statement of Questions Presented

1. Is the requirement of separation of ''person'' and ''enterprise'' under Section 1962(c) of the RICO statute, 18 U.S.C. § 1962(c), satisfied where the ''enterprise'' is alleged to consist of a corporation and its subsidiaries and agents, and the ''persons'' named as defendants are the corporation, two of its subsidiaries, and two of their employees?

2. Did cross-petitioner succeed in alleging any predicate acts in violation of 18 U.S.C. § 1962(c)?

3. Was cross-petitioner injured in its business or property, within the meaning of 18 U.S.C. § 1964(c), by reason of any alleged violation of 18 U.S.C. § 1962(c)?

## Statement Pursuant to Supreme Court Rule 29.6

Pursuant to Supreme Court Rule 29.6, the corporate cross-respondents state that cross-respondent NYNEX Corporation has no parent company, and that it is the direct or indirect parent company of cross-respondents New York Telephone Company and NYNEX Materiel Enterprises Company. New York Telephone Company and NYNEX Materiel Enterprises Company have no nonwholly owned subsidiaries. The nonwholly owned entities in which NYNEX Corporation has direct and indirect interests are listed on pages ii-iii of the initial Petition for a Writ of Certiorari in this case, No. 96-1570.

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ON CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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## BRIEF IN OPPOSITION TO CONDITIONAL CROSS-PETITION

Discon Incorporated ("Discon"), the respondent in No. 96-1570, has filed a conditional cross-petition for certiorari. For the reasons summarized below, Discon's conditional cross-petition should be denied.

The issues raised in Discon's conditional cross-petition have no relationship to the issues raised in the initial petition for certiorari in this case. The initial petition for certiorari challenges the unprecedented theories adopted by the court below under Sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1, 2, which are in direct conflict with holdings of this Court and numerous Courts of Appeals. The cross-petition questions the lower court's application of Section 1962(c) of the RICO statute, 18 U.S.C. § 1962(c). As shown below, the

lower court's application of Section 1962(c) was correct, and is supported by the weight of relevant authority in the Courts of Appeals, which Discon fails to cite in its cross-petition. In addition, Discon's Section 1962(c) claim was properly dismissed because it failed to allege the required predicate acts and injury to its business or property by reason of a violation of Section 1962(c).

## Statutes Involved

Section 1962(c) of the RICO statute, 18 U.S.C. § 1962(c), reads as follows:

> "It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt."

Section 1964(c) of the RICO statute, 18 U.S.C. § 1964(c), reads in pertinent part as follows:

> "Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee . . . ."

## Counter-Statement of the Case

### A. Discon's Section 1962(c) Claim

Discon's initial complaint alleged violations of all four subsections of the RICO statute, 18 U.S.C. § 1962(a), (b), (c), and (d) (JA52-JA55[1]). The District Court dismissed these claims on numerous grounds, but granted leave to replead (JA70-JA71, JA86-JA97, JA108).

Discon's amended complaint did not include the claim under 18 U.S.C. § 1962(a), but sought to replead the claims under 18 U.S.C. § 1962(b), (c), and (d) (JA152-JA157). Discon's Section 1962(c) claim alleged that the "enterprise" consisted of NYNEX Corporation ("NYNEX") and its subsidiaries, as well as "attorneys, accountants and other agents" (JA152). It alleged that the defendant "persons" who supposedly conducted and participated in the affairs of the enterprise through a pattern of racketeering activity were NYNEX, two of its subsidiaries (NYNEX Materiel Enterprises Company ("MECo") and New York Telephone Company ("NYT")), and two of their employees (Robert J. Eckenrode and Bernard O'Reilly) (*id.*).

Discon alleged a pervasive pattern of racketeering activity on the part of NYNEX and its subsidiaries and their employees (JA152-JA153). It alleged that a key part of this pattern of racketeering activity consisted of excessive payments by NYT to other NYNEX companies, which were alleged to be part of a scheme to defraud regulatory commissions and ratepayers (JA113, JA132-JA139). Despite this allegation of fraud on regulatory commissions, Discon's amended complaint admitted that regulatory commissions

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1. "JA" citations are to the Joint Appendix in the Court of Appeals.

were aware that NYT's payments to other NYNEX companies included markups, and actively investigated those payments.[2] Discon's amended complaint also alleged a variety of other RICO predicate acts, including obstruction of justice and extortion (JA113, JA139-JA147).

**B. The Decision of the District Court**

The District Court dismissed the RICO claims in Discon's amended complaint on multiple and independently sufficient grounds (Pet. 38a-49a).

First, the District Court held that Discon had failed to allege RICO predicate acts that injured it in its business or property (Pet. 40a-46a). In particular, the District Court held that Discon had failed to plead the alleged fraud-based predicate acts with the particularity required by Federal Rule of Civil Procedure 9(b), and had failed to allege any fraud directed at Discon (Pet. 40a-44a). The District Court also held that Discon had failed to plead predicate acts of extortion and obstruction of justice (Pet. 45a-46a).

Second, the District Court held that Discon had failed to satisfy the specific requirements of the RICO subsections it relied upon (Pet. 47a-49a). With respect to Section 1962(c), the District Court held that Discon had failed to allege an "enterprise" that was distinct from the "persons" named as defendants, as required by Section 1962(c) (Pet. 48a-49a).

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2. The Federal Communications Commission ("FCC") began an investigation in mid-1988 which led in February 1990 to the FCC order to show cause which is referred to in the amended complaint (*see* JA120-JA121) and in the cross-petition (*see* Cr.-Pet. 3). The New York State Public Service Commission ("NYPSC") conducted an audit, referred to in the amended complaint (*see* JA130), which led to a November 1987 report recommending that MECo's prices to NYT be adjusted to reflect a rate of return for MECo that would be no higher than that authorized for NYT.

## C. The Decision of the Court of Appeals

The Court of Appeals held that the District Court had properly dismissed Discon's RICO claims for failure to satisfy the specific requirements of 18 U.S.C. § 1962(b), (c), and (d) (Pet. 15a-20a).

With respect to Section 1962(c), the Court of Appeals noted (Pet. 17a) that it had previously held that Section 1962(c) clearly requires that the "person" and the "enterprise" be distinct, *Bennett* v. *United States Trust Co.*, 770 F.2d 308, 315 (2d Cir. 1985), *cert. denied*, 474 U.S. 1058 (1986), and that this requirement cannot be circumvented "by alleging a RICO enterprise that consists merely of a corporate defendant associated with its own employees or agents carrying on the regular affairs of the defendant . . . ." *Riverwoods Chappaqua Corp.* v. *Marine Midland Bank*, 30 F.3d 339, 344 (2d Cir. 1994).

The Court of Appeals held in the present case that the requirement of a distinction between the "person" and the "enterprise" under Section 1962(c) of the RICO statute likewise cannot be circumvented by alleging an enterprise consisting of the defendant corporation and its wholly-owned subsidiaries (Pet. 18a-19a).

## REASONS FOR DENYING THE WRIT

### I. The Court of Appeals Correctly Held That the Requirement of a Distinction Between the "Person" and the "Enterprise" Under Section 1962(c) of the RICO Statute Is Not Satisfied Where the "Person" and the "Enterprise" Both Consist of a Corporation and Subsidiaries and Employees of the Corporation

Section 1962(c) of the RICO statute (quoted on page 2 above) draws a clear distinction between the defendant "person" and the "enterprise." As a result, "[v]irtually all courts of appeals considering the question hold that, as a matter of law, the same person may not be both a section 1962(c) enterprise and a defendant." Douglas E. Abrams, *The Law of Civil RICO* § 4.7.1, at 223 (1991) (footnote omitted).[3] Thus, for example, a corporation such as NYNEX cannot be both the "person" and the "enterprise" under Section 1962(c).

In its Section 1962(c) claim, Discon sought to avoid this requirement by defining the "enterprise" as including NYNEX and its subsidiaries, and by naming as the defendant

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3. *See, e.g.*, *Bennett* v. *United States Trust Co.*, 770 F.2d 308, 315 (2d Cir. 1985), *cert. denied*, 474 U.S. 1058 (1986); *Atkinson* v. *Anadarko Bank & Trust Co.*, 808 F.2d 438, 439 (5th Cir.), *cert. denied*, 483 U.S. 1032 (1987); *Haroco, Inc.* v. *American Nat'l Bank & Trust Co.*, 747 F.2d 384, 399-402 (7th Cir. 1984), *aff'd per curiam on other grounds*, 473 U.S. 606 (1985); *Bennett* v. *Berg*, 685 F.2d 1053, 1061-62 (8th Cir. 1982), *aff'd in part, rev'd in part on other grounds en banc*, 710 F.2d 1361 (8th Cir.), *cert. denied*, 464 U.S. 1008 (1983).

The only Court of Appeals that has held to the contrary appears to be the Eleventh Circuit. *See, e.g.*, *United States* v. *Hartley*, 678 F.2d 961, 986-90 (11th Cir. 1982), *cert. denied*, 459 U.S. 1170, 1183 (1983).

"persons" NYNEX, two of its subsidiaries, and two of their employees (JA152). The court below held that this did not supply the required distinction between the "person" and the "enterprise," because a corporation such as NYNEX necessarily carries on its activities through subsidiaries and employees (Pet. 17a-19a).

Discon's cross-petition argues that this holding was in conflict with the decisions of nine other Circuits (Cr.-Pet. 6-8 & n.2). In actuality, the holding of the court below is consistent with the weight of authority in the Circuits that have addressed this issue.[4] The cases cited by Discon either did not

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4. *See, e.g.*, *Compagnie de Reassurance d'Ile de France* v. *New England Reinsurance Corp.*, 57 F.3d 56, 92 (1st Cir.) (wholly-owned subsidiary not distinct from alleged parent-enterprise), *cert. denied*, 116 S. Ct. 564 (1995); *Odishelidze* v. *Aetna Life & Cas. Co.*, 853 F.2d 21, 23 (1st Cir. 1988) ("the Aetna companies and their officers or employees (the named defendants) cannot be the entity that conducts its own affairs through a pattern of racketeering activity"); *NCNB Nat'l Bank* v. *Tiller*, 814 F.2d 931, 936 (4th Cir. 1987) (bank subsidiary not distinct from alleged holding company-enterprise); *United States* v. *Computer Sciences Corp.*, 689 F.2d 1181, 1190-91 (4th Cir. 1982) (en banc) (division not distinct from alleged corporation-enterprise), *cert. denied*, 459 U.S. 1105 (1983); *Parker & Parsley Petroleum Co.* v. *Dresser Indus.*, 972 F.2d 580, 583-84 (5th Cir. 1992) (RICO enterprise may not consist of "the defendant corporate entity functioning through its employees in the course of their employment"); *Old Time Enters., Inc.* v. *International Coffee Corp.*, 862 F.2d 1213, 1217-18 (5th Cir. 1989) ("Nor does the fact that individual officers and employees of a corporation, in the course of their employment associate together and commit in the conduct of the corporation's business a pattern of predicate acts in its name and on its behalf, suffice to constitute such officers and employees (alone or together with the corporation itself) an association in fact enterprise distinct from the corporation."); *Atkinson* v. *Anadarko Bank & Trust Co.*, 808 F.2d 438, 440-41 (5th Cir.) (alleged association of bank, its holding company, and three employees not distinct from bank), *cert. denied*, 483 U.S. 1032 (1987); *Puckett* v. *Tennessee Eastman Co.*, 889 F.2d 1481, 1489 (6th Cir. 1989) (plaintiff's claim "contemplated only one entity, the corporation, acting in the only manner it is

involve the issue presented here, which is whether the "person" and the "enterprise" are distinct when both of them include a corporation and subsidiaries and employees carrying on the activities of the corporation,[5] or did not squarely address the reasoning of the cases cited in footnote 4 above.[6]

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possible for a corporation to act, through its employees"); *Richmond* v. *Nationwide Cassel L.P.*, 52 F.3d 640, 647 (7th Cir. 1995) (plaintiff cannot "circumvent the distinctiveness requirement by alleging enterprises that are merely combinations of individuals or entities affiliated with a defendant corporation"); *Board of County Comm'rs of San Juan County* v. *Liberty Group*, 965 F.2d 879, 886 (10th Cir.) ("the officers and employees of an organization cannot, in the ordinary course of their duties, constitute an association in fact separate from the organization itself"), *cert. denied*, 506 U.S. 918 (1992).

5. Most of the cases cited by Discon did not involve an "enterprise" and "persons" both of which consist of a corporation and subsidiaries and employees of the corporation (*see* Cr.-Pet. 7-8 n.2).

6. The Third Circuit has rendered inconsistent decisions, first holding that employees and affiliates of a corporation are not distinct from the corporation for purposes of Section 1962(c), *see, e.g.*, *Brittingham* v. *Mobil Oil Corp.*, 943 F.2d 297, 300-03 (3d Cir. 1991), and then holding that employees may be distinguished from the corporation. *See Jaguar Cars, Inc.* v. *Royal Oaks Motor Car Co.*, 46 F.3d 258, 268-69 (3d Cir. 1995), cited by Discon (Cr.-Pet. 7 n.2). Even after *Jaguar Cars*, the Third Circuit affirmed a holding that a corporation is not distinct from an "enterprise" including its subsidiaries and affiliates. *See Metcalf* v. *PaineWebber Inc.*, 886 F. Supp. 503, 512-15 (W.D. Pa. 1995), *aff'd without opinion*, 79 F.3d 1138 (3d Cir. 1996).

The Third Circuit panel in *Jaguar Cars* suggested that its holding was required by *Reves* v. *Ernst & Young*, 507 U.S. 170 (1993). *See* 46 F.3d at 268-69. This suggestion was erroneous. In *Reves*, this Court held that, to be liable under RICO Section 1962(c), a defendant "person" must participate in the operation or management of the "enterprise." *See* 507 U.S. at 177-86. *Reves* did not address the contours of the required distinction between the "person" and the "enterprise," and did not suggest that a Section 1962(c) claim can be sustained where both the "person" and the "enterprise" include a corporation and subsidiaries and employees of the corporation.

The holding of the court below on the issue presented in this case was clearly correct. If Discon's argument were valid, then all a plaintiff would need to do in order to circumvent the distinctiveness requirement of Section 1962(c) in any claim against a corporation would be to name as a defendant at least one employee or subsidiary of the defendant corporation. This would reduce the distinctiveness requirement to a dead letter in any case involving a corporation.

Discon argues that the holding of the court below undermines "[t]he bedrock purpose of RICO . . . to prevent the turning of legitimate businesses to criminal ends" (Cr.-Pet. 10). This argument proves far too much. If it had been the purpose of Congress to make available a treble damage remedy for any alleged federal or state crime, it would have been a simple matter to draft a statute saying just that. Congress did not do so. Instead, it provided a treble damage remedy under RICO only where the requirements of one of the subsections of Section 1962 of the RICO statute are met. In the case of Section 1962(c), one of the most important of these requirements is the distinctiveness requirement. The court below correctly enforced the distinctiveness requirement in this case.

## II. As the District Court Properly Held, Discon's Section 1962(c) Claim Is Also Subject to Dismissal for Additional and Independent Reasons

The issue which Discon seeks to tender to this Court in its cross-petition is not determinative of the fate of its Section 1962(c) claim. As the District Court held, Discon's Section 1962(c) claim is independently subject to dismissal because Discon failed to allege RICO predicate acts, and because it failed to allege injury to its business or property by reason of

any such acts (Pet. 40a-46a).[7]

### A. Discon Failed to Allege Any RICO Predicate Acts

In order to state a claim for damages based on an alleged violation of Section 1962(c), a plaintiff must allege that it has been injured in its business or property by reason of RICO predicate acts. *Sedima, S.P.R.L.* v. *Imrex Co.*, 473 U.S. 479, 496 (1985). The District Court correctly held that plaintiff had failed to meet this requirement (Pet. 40a-46a).

Discon relied principally upon alleged predicate acts of mail fraud, wire fraud, and securities fraud (JA113, JA132-JA139, JA142-JA144). The District Court held that Discon had failed to state "the circumstances constituting fraud . . . with particularity," as required by Federal Rule of Civil Procedure 9(b) (Pet. 40a-44a). This holding was clearly correct. To comply with Rule 9(b), a complaint alleging fraud must "(1) specify the statements that the plaintiff contends were fraudulent, (2) identify the speaker, (3) state where and when the statements were made, and (4) explain why the statements were fraudulent."[8] The District Court held, after a careful review of Discon's "confusing and lengthy" amended complaint (Pet. 50a), that Discon's allegations failed to satisfy this standard (Pet. 42a-44a).[9]

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7. Because the Court of Appeals held that Discon had failed to satisfy the specific requirements of Section 1962(b), (c), and (d), it did not reach these alternative grounds for dismissal (*see* Pet. 15a-20a).

8. *Shields* v. *Citytrust Bancorp., Inc.*, 25 F.3d 1124, 1128 (2d Cir. 1994), *quoting Mills* v. *Polar Molecular Corp.*, 12 F.3d 1170, 1175 (2d Cir. 1993), *citing Cosmas* v. *Hassett*, 886 F.2d 8, 11 (2d Cir. 1989).

9. The defectiveness of Discon's fraud allegations was particularly obvious in light of the admitted fact that the regulatory commissions, which were allegedly defrauded, were aware of MECo's markups and were actively investigating them (*see* pp. 3-4 & n.2 *supra*).

The District Court also held that Discon had failed to allege predicate acts of extortion and obstruction of justice (Pet. 44a-46a). Again, these holdings were correct.

### B. Discon Failed to Allege Injury to Its Business or Property by Reason of Any RICO Predicate Acts

Section 1964(c) of the RICO statute provides that, in order to recover treble damages, a plaintiff must be "injured in his business or property by reason of a violation of" Section 1962. Section 1964(c) requires that the injury to business or property be the direct and proximate result of the RICO violation. *Holmes* v. *SIPC*, 503 U.S. 258, 265-70 (1992).

Discon claimed that it was injured in its business or property by the alleged fraud in its capacity as a telephone ratepayer, but the District Court correctly held that this claim was barred by the filed rate doctrine, since the telephone rates paid by Discon were regulated by federal and state regulatory commissions (Pet. 46a).[10] Discon also alleged that the NYNEX companies stopped dealing with it so that they could maximize their profits from the alleged fraud, but such an indirect and speculative chain of causation running from the alleged fraud to the alleged injury does not satisfy the requirements of Section 1964(c) of the RICO statute (*see* Pet. 44a).[11]

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10. *See, e.g., Sun City Taxpayers' Ass'n* v. *Citizens Utils. Co.*, 45 F.3d 58, 61-62 (2d Cir.), *cert. denied*, 115 S. Ct. 1693 (1995); *Wegoland Ltd.* v. *NYNEX Corp.*, 27 F.3d 17, 19-22 (2d Cir. 1994); *Taffet* v. *Southern Co.*, 967 F.2d 1483, 1488-95 (11th Cir.) (en banc), *cert. denied*, 506 U.S. 1021 (1992); *H.J., Inc.* v. *Northwestern Bell Tel. Co.*, 954 F.2d 485, 488-94 (8th Cir.), *cert. denied*, 504 U.S. 957 (1992).

11. Thus, for example, former employees who allege that they have been terminated for reporting or refusing to participate in a pattern of racketeering activity lack standing to assert a RICO claim. *See, e.g., Bowman* v. *Western Auto Supply Co.*, 985 F.2d 383, 385-86 (8th Cir.), *cert. denied*, 508 U.S. 957 (1993); *Willis* v. *Lipton*, 947 F.2d 998,

Similarly, Discon failed to allege that it was injured in its business or property by reason of the alleged predicate acts of extortion and obstruction of justice (*see* Pet. 44a-46a).

Thus the dismissal of Discon's claim under Section 1962(c) of the RICO statute was proper, and should be affirmed, regardless of the issue which Discon seeks to present to this Court in its conditional cross-petition for certiorari.

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1000-01 (1st Cir. 1991); *Reddy* v. *Litton Indus., Inc.*, 912 F.2d 291, 294 (9th Cir. 1990), *cert. denied*, 502 U.S. 921 (1991); *Kramer* v. *Bachan Aerospace Corp.*, 912 F.2d 151, 154-56 (6th Cir. 1990); *Hecht* v. *Commerce Clearing House, Inc.*, 897 F.2d 21, 24 (2d Cir. 1990); *Burdick* v. *American Express Co.*, 865 F.2d 527, 529-30 (2d Cir. 1989).

Similarly, as the District Court held (Pet. 44a), a fraud-based RICO claim can be maintained only by the direct targets of the alleged fraud. *See, e.g., Israel Travel Advisory Serv., Inc.* v. *Israel Identity Tours, Inc.*, 61 F.3d 1250, 1257-58 (7th Cir.), *cert. denied*, 116 S. Ct. 1847 (1995); *Central Distribs. of Beer, Inc.* v. *Conn*, 5 F.3d 181, 184 (6th Cir. 1993), *cert. denied*, 114 S. Ct. 2678 (1994).

## CONCLUSION

For the reasons set forth above, cross-petitioner's conditional petition for a writ of certiorari should be denied.

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Respectfully submitted,

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